



USDA Foreign Agricultural Service

GAIN Report

Global Agriculture Information Network

Template Version 2.09

Voluntary Report - Public distribution

Date: 8/28/2008

GAIN Report Number: CH8812

China, Peoples Republic of Agricultural Situation

Hefei: An Emerging City Market in Central China 2008

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Report Highlights:

As a key city in the government's proposed expansion plan of the Yangtze River Delta Economic Region, Hefei is well-positioned to capture the industrial shift from coastal areas into China's interior. In 2007, Hefei's GDP reached US\$19 billion, an increase of nearly 20% from the previous year. Driven by its strong economy, consumer demand is noticeably rising. ATO Shanghai conducted interviews with managers from the HRI, retail and wholesale sectors, and discovered that current sales of imported foods are comparatively limited. Nevertheless, the major retailing giants like Metro, Wal-Mart, and Carrefour have already entered this market and increasingly, local high-end restaurants are also using imported products, all factors which will promote the distribution of imported foods and increase familiarity of Western ingredients and condiments among end consumers. This indicates a considerable upside potential for market expansion and development for U.S. agricultural products.

Includes PSD Changes: No
Includes Trade Matrix: No
Annual Report
Shanghai ATO [CH2]
[CH]

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I. Hefei--Anhui Provincial Capital City

Hefei, the capital of Anhui Province, is located in the central region of China between the Yangtze and Huaihe Rivers and adjacent to Chaohu Lake, which is one of the five great freshwater lakes in China. There are four urban districts under the city's jurisdiction: Yaohai, Luyang, Shushan and Baohe Districts; three counties: Feidong, Feixi and Changfeng Counties; three development zones: *Hefei State New & High Technology Industrial Development Zone*, *Hefei Economic and Technological Development Area (HETDA)* and *Hefei New Railway Station Comprehensive Development Experimental Zone*. With nearly 40 per cent of its total area in greenery, Hefei is regarded as one of the "National Garden Cities" in China.



Hefei urban view

As an important base for science and education in China, Hefei plays an important role in scientific research. It has three national laboratories, second only to Beijing: the National Synchrotron Radiation Laboratory under the University of Science and Technology of China, the Hefei National Laboratory for Physical Sciences and the National Laboratory for Nuclear Fusion Research both of which are under the Hefei Institute of Physical Sciences, Institute of Plasma Physics, which itself is under the Chinese Academy of Sciences. The world-renowned *University of Science and Technology of China (USTC)* and the Hefei Branch of the *Chinese Academy of Sciences (CAS)* are also both in the city.

Hefei is the center of Anhui province's politics, economy, science, education, culture and transportation, a rapidly growing industrial city with textile mills, ironworks and steelworks, chemical and food processing plants and a variety of other manufacturers. Fortune 500 companies located in Hefei include Coca-Cola, ABB, Unilever, Hitachi, Sanyo, Metro, and Carrefour. Famous Chinese domestic companies including JAC, Haier, Midea, Changhe, Changhong, Gree, Yili, etc. have also made investments in Hefei.

As a key city in the government's proposed expansion plan of the Yangtze River Delta (YRD) Economic region, Hefei is well-positioned to capture the industrial shift from China's coastal areas into the interior. Its GDP reached US\$19 billion in 2007, an increase of nearly 20% from the previous year. The yearly import and export volume totaled US\$6.25 billion,

increased by 28.2%, of which export volume was US\$4.3 billion with an increase of 26.3%, import volume was US\$1.95 billion with an increase of 32.6%. The services sector represented about 45% of Hefei's GDP. This sector includes finance and insurance, transportation and communication, wholesale and retail sales and catering.

A. Hefei at a glance (2007)

1. HEFEI CITY AREA	7,029 SQUARE KILOMETERS
2. Urban Area	820 square kilometers
3. Population	4.8 million
4. Urban Population	2.6 million
5. GDP	US\$19.0 billion
6. GDP Growth Rate (2007)	19 %
7. Per Capita GDP	US\$4,005
8. Urban household Expenditure	42.6% on Food
9. Major Industries	Automotive; machinery; household electronics and products; manufacturing; food processing; chemicals, tires; IT and software; biotechnology
10. Academic and Intellectual Resources	30 universities and more than 190 scientific research institutions
11 Star-rated Hotels	4 five-star, 9 four-star and 19 three-star
12. Major Food Retailers	Metro, Joy-Mart, Carrefour, Wal-Mart, Lotus
13. Key Agricultural Products	freshwater fish/ lobsters , cotton, pork, dairy, poultry, vegetables

Chart 1. Source: Hefei Investment Promotion Bureau

B. Transportation – One of the Key Hubs in China

Hefei possesses a strategically important location easily accessible from all directions of the country; it is a comprehensive transportation hub in central China.

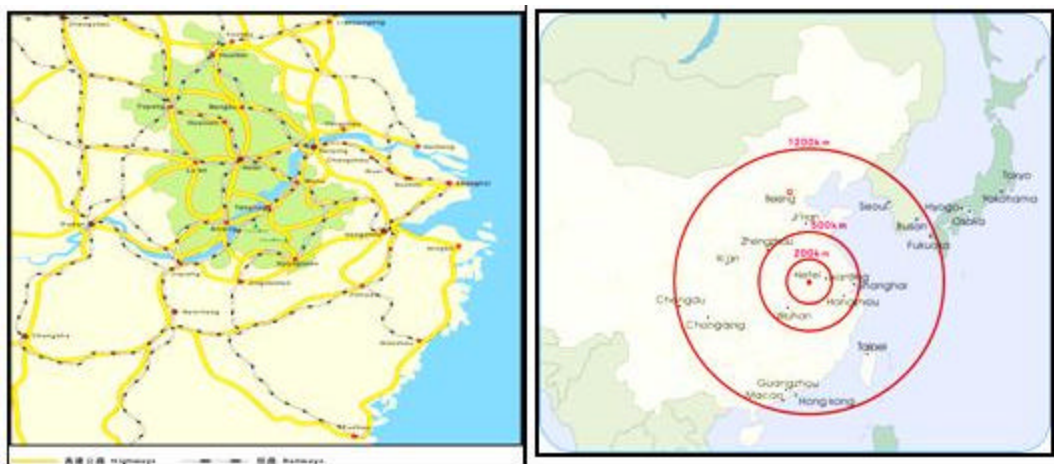
a. Airport: There are more than 30 domestic and international air routes connecting the city with the outside, the new 4E-level international airport is expected to be completed at the end of 2008; by then, Hefei will have airlines connections to more major cities worldwide.

b. Ports: Hefei Port is about 430km from Shanghai Port, 150km from Nanjing Port and 140km from Wuhu Port. Through the Fei River and Chaohu Lake, with a capability of handling

500-1,000 MT cargo barges, Hefei is a link to port cities along the Yangtze River. After the completion of a canal connecting the Yangtze and Huaihe rivers, Hefei will become an important water transportation hub. Now that Hefei Customs has joined Yangtze River Delta in realizing a regional Customs clearance operation, enterprises in Hefei's Economic and Technological Development Area can now ship through the three ports efficiently.

Photo 2. Transportation map of Hefei (left);

Photo 3. Economic Area within a Radius of 500 km of Hefei (right).



Source: The Administration Commission of Hefei Economic and Technological Development Area

c. Railway: The Hefei-Jiujiang and Beijing-Kowloon railways as well as the Nanjing–Xi'an and Shanghai-Chengdu railways intersect in Hefei, which makes it an important link in the railway network in the country. An express railway, which was completed in 2007, reduced the travel time to Shanghai from 7 hours to 2.5 hours, and the time to Nanjing to only 45 minutes. The Hefei-Bengbu section of the Beijing-Shanghai express railway is under construction, and is expected to be completed in three to five years and will cut travel time to four hours from Hefei to Beijing.

d. Highway: A network of expressways connects the major cities in east China, including Nanjing, Shanghai, Wuxi, Changzhou, Hangzhou, Wuhan, Xuzhou, etc. which makes Hefei not only the transportation hub in Anhui province, but also a highway transportation center in the country.

C. HETDA

HETDA (Hefei Economic & Technological Development Area) is an important component of the local economy. Since 2002, it has accounted for over one-third of the Hefei's total industrial output. By the end of 2007, 2024 international enterprises had settled in Hefei, HETDA had utilized a total of US\$1.76 billion in foreign direct investment (FDI).

There are six special parks/zones in HETDA, the Micro-Electronic Engineering Zone (MEEZ), the Sinotrans Logistic Park (SLP), the Italian Industry Zone (IIZ) and the Housing Industrialization Base (HIB) are currently operating; the Life Science Zone (LSZ) and the Nanyan Lake High-Tech Zone (NLHTZ) are still under construction.

With a full catalog of industries and supporting facilities, HETDA is a new thriving industrial base; eight key industries have taken shape, comprising auto-making, equipment manufacturing, house-hold appliance, chemical industry and tires, IT and software, new materials, biotechnology and new medicines and food processing. Coca-Cola, Uni-President, Huatai and Chia Tai are among the many food processing companies located in this area.

D. Binhu—Lakeside New City District

The Binhu (lakeside) new area covering more than 824 acres, features a unique "lakeside" culture; it will function as a new administrative, commercial, exhibition center and will contain a comprehensive and expansive residential area. All the projects in this new area are to be completed by 2010, including new schools, hospitals, banks, government institutional buildings, shopping malls, star-rated hotels, etc. Following are two examples:

- Covering an area of 16 acres and a total investment of RMB350 million, the Anhui Agricultural Service Center includes the Quality Safety Supervision and Test Center for farm products under the Ministry of Agriculture, the Anhui Agricultural Technology Department Center, the Anhui Agricultural Exhibition Hall and the Anhui Agricultural Technology Center, all projects to be completed by 2010.
- Binhu Century Town, an extremely large real estate project with a total investment exceeding RMB 12billion, will combine residential and commercial projects, a 5-star hotel and a shopping mall. This project is partially completed.

II. Sector Analysis

A. Hefei's local Agriculture

In 2007, the total annual grain output was 1.95 million tons, an increase of 8.4% over the previous year. For crops, cotton output increased by 17.1%, to 21,000 tons, and oil-bearing crops sank 8.6% to 293,000 tons, while the yield of vegetables amounted to 939,000 tons, showing an increase of 19%. Animal husbandry and aquaculture sector saw stable growth. Aggregated annual meat production reached 395,000 tons, an increase of 7.9% over the previous year. Egg production increased by 6.1% while the aquatic output increased by 8.2% amounting to 143,000 tons.

Livestock is an important part of Anhui's agricultural sector; Chun Ran is the largest swine farm in Hefei with an annual output of over 100,000 head. The farm is a pork supplier for local consumers as well as for the Shanghai market. Yili Group in Hefei provides management support for cow breeders, its reach covering about 30,000 small farms.

Lobster: Hefei's aggregated annual production of lobster reached 26,000 tons last year, farmed over an area of 62,000 acres. Hefei is recognized as China's fresh water lobster breeding capital. Thirty-nine new farms, each with an area of over 200 acres were built with the support of the local government. Hefei hosts an annual lobster festival with features art performances and trade exhibitions.

B. Food Processing

Focusing on processing poultry, tea, dairy and grain products, during the last few years, Hefei's food processing industry has seen a rapid development. Yili Group, Huatai Group and Unilever are the most well-known local food processing enterprises. Inner Mongolia Yili Industrial Group Co., Ltd. is a leading enterprise in China's dairy industry. In 2007, Yili Group's primary revenue reached 20 billion RMB and total profits increased by 27% compared with the same period during the previous year. Some of the company's high-tech and value-added products include milk powder and ice-cream. These, among the company's more profitable products are manufactured in a subsidiary company located in Hefei, and result in a high demand for U.S. whey in the area.

QiaQia brand roasted seeds are produced by the Anhui Provincial Qiaqia Co., Ltd, a company with five production bases, 60 branches and offices. The company's headquarters is located

in Hefei and is the largest roasted seed and nuts enterprise in China. Hefei hosts the largest national annual roasted snack fair as well.

Hefei is also famous for its Feixi chicken. According to the Hefei Livestock Breeding Bureau, the Anhui Hewei Group has invested in a large-scale chicken meat processing center in Hefei. By the time this project is completed, it could be the biggest chicken/ by-products processing factory in the world, with a capacity to process 650,000 chickens per day, or about 240 million per year and an estimated yearly revenue of RMB 6 billion.

C. HRI & Cuisine

Hefei is the northern gateway to the renowned Yellow Mountains, and its surrounding area abounds with tourist attractions. There are many famous sites known nation-wide within 300 kilometers of the city, including the Yellow Mountains, Mt. Jiuhua, Taiping Lake, Mt. Tianzhu, Mt. Tiantangzhai, Mt. Langya as well as the ancient town of Shouxian and a Ming Dynasty Imperial Mausoleum. With over 30 regional tourist attractions, Hefei is an ideal mid-way destination for tourists from northern China who are headed towards tourist attractions in the south and east of the country.

Hefei was awarded the title of "China's Top Tourist City." In recent years, the scale of the city's tourist industry has steadily expanded, its tourist infrastructure has continuously improved, and the construction of tourist attractions has accelerated, which has greatly enriched the content of Hefei tourism. According to the Hefei Development and Reform Commission, together with the city's already existing four 5-star, nine 4-star and nineteen 3-star hotels in Hefei city, 95 travel services and 8 international travel services, several international recognized brand hotels have recently decided to start operations in the city.

Chart 2. Hefei Hotels & High-end Restaurants

Hotels	Notes
1. Hilton Hefei (5 star)	<i>Features the Phoenix, Sens, Happy Panda and Indigo restaurants, as well as the coffee & snack bar Café Cino which combines Western & Eastern cuisine</i>
2. Holiday Inn Hefei (5 star)	<i>29th floor Western restaurant with a capacity for 400 guests</i>
3. Sofitel Grand Park Hefei(5 star)	<i>Brazilian style restaurant and Western style garden Café</i>

4. Grand Hotel Oversea Traders Club(5 star)	<i>Includes a Chinese restaurant, Western restaurant, lobby bar, and an executive floor bar</i>
5. Hefei International Peace Hotel (4 star)	<i>Cantonese, Huaiyang, Anhui and Chao cuisines and Brazilian BBQ restaurants</i>
6. New Wencai International Hotel (4 star)	<i>Chinese cuisine, tea house, Japanese cuisine</i>
7. Anhui Hotel (4 star)	<i>Features Anhui, Huaiyang, Cantonese and Western cuisine</i>
8. Novotel Hefei (4 star)	<i>Two restaurants and one European style bar</i>

Source: Hefei Commercial Bureau

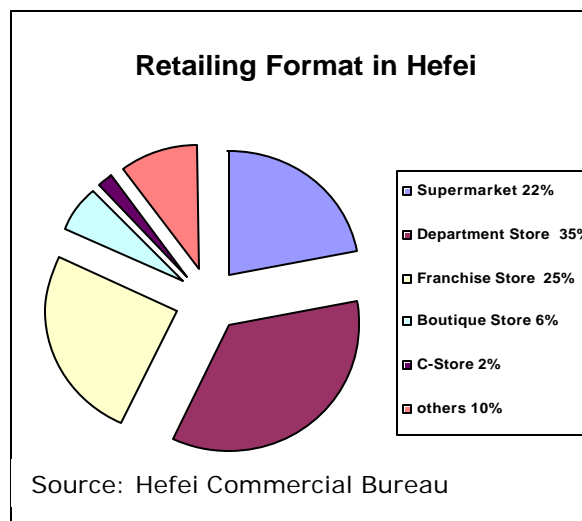
Western cuisine restaurants/bars located in high-end hotels are the major consumers of imported food ingredients and condiments; high-quality imported food and beverages are available at luxurious restaurants and bars such as the Phoenix, Sens, Happy Panda and Indigo, venues which provide a combination of Western and Eastern cuisine. Wines are mainly imported from France and Australia. Very few California wines appear in the market, the main reason being that local chefs are unaware of American products, and an undeveloped distributional channel which relies heavily on Shanghai-based distributors. One executive chef from a hotel in Hefei admitted that U.S. beef products are used at the hotel, obtained through gray distribution channels. U.S. frozen potato products are widely used in these restaurants and bars, as well as Western style fast-food chains; frozen gold crisp onion rings, sweet corn and frozen mixed vegetables are becoming increasingly popular. American tabasco sauce and tomato catsup products are already present in the local supermarkets, and are generally purchased by hotels and restaurants.

Local cuisine is called Hui cuisine, and it is one of the famous eight Chinese cuisines, with an emphasis on strong color and flavor; meat or fish dishes are often prepared using special steam or stew cooking methods with generous use of sauces and oil. Shu Wang Group and Jing Man Lou Group are the local top local restaurant chains. According to the Commercial Bureau of Hefei, in 2007, there were five local restaurant chains with yearly sales reaching 20 million RMB. Hefei people are usually willing to try new flavors, and Hui cuisine itself developed though incorporating elements from China's other seven regional cuisines. Furthermore, local chefs like to innovative and frequently use imported ingredients and condiments to enrich their menus and stand out from the competition.

D. Food Wholesale & Retail Sector

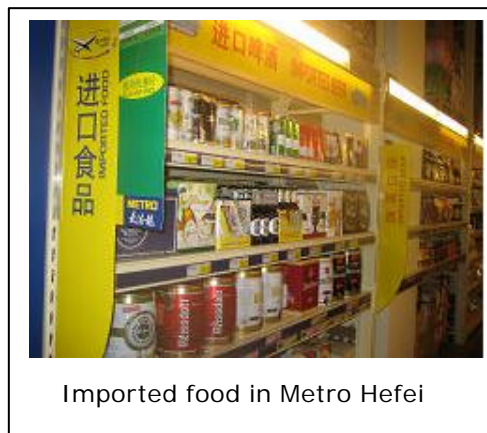
Major provincial consumer markets are located in Hefei. In 2007, retail sales of consumer goods rose by 22% to RMB 46.9 billion. There are about 46,000 commercial retail outlets in the city, including 33 large-scale markets, whose shopping floors cover over 5,000 square meters. Retailing giants like Metro, Wal-Mart and Carrefour already operate shopping malls and supermarkets in Hefei city. The biggest local retailer is Store Group, and one of its

subsidiaries Joy-Mart supermarkets has a successful local operation in the area. Tesco is the latest to enter this market, and will open the first of a planned five stores in Hefei by the end of 2008. These enterprises overall are optimistic about the future of the Anhui markets, especially in the capital city of Hefei.



a. Metro Cash & Carry

Metro, the world's leading self-service wholesale business, opened its first store in Hefei on November 2007, becoming the 35th Cash & Carry market in China. The new store covers 6,155 square meters of business space with over 23,000 food and non-food items. The Metro store in Hefei stocks 1,723 imported food products and approximately 200 SKUs originally from the U.S., accounting for 12.3% of retailed goods; among them, fruits and vegetables account for 24.3%, seafood 5.2%, frozen food products 19%, wine 6.6%, beers & other beverages 17%, and dairy products 5%. The store's



target customers are categorized into three groups-HoReCa (hotels, restaurants and caterers); traders and complementary business units. The store recruited over 80,000 registered professional customers before the store even opened for business.

b. Zhougudui Wholesale Market

As one of the subsidiaries of Hefei Department Store Group, Zhougudui agricultural products wholesale market was originally built as a fruit market. Backed by the Hefei Zhougudui Wholesale Market Ltd., it originally covered an area of 10 acres in 1992. After ten years, it developed into a large-scale agricultural products distribution center, with an area of 280 acres. Besides a fruit and vegetable section, the market includes aquatic products, meat, poultry and egg products, as well as condiments and a cooking oil section. Last year, the market had a total turnover of over RMB 7 billion with a sales volume over 2.2 million tons. The Zhougudui management team is making a great effort to advance their existing services and increase their competitive capabilities. Zhougudui has expanded into a multi-functional market, combining agricultural exhibitions, food safety controls, and an international-standard agricultural product logistic and food processing center. Its development has been facilitated by its adaption of an E-balance system to monitor and control its business transactions.

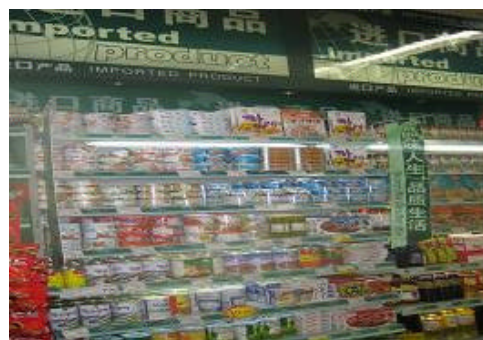
Chart4. **Hefei Major Food Retailers**

Name	Format	Number of outlet
Metro Cash & Carry	Hypermarket	1
Carrefour	Hypermarket	3
Wal-Mart	Hypermarket	1
Lotus	Hypermarket	1
Parkson	Supermarket	1
Hefei Department Stores (CBD)	Department Store	1
Trust-Mart	Supermarket	2
Suguo	Supermarket	6
Beijing Hualian	Supermarket	3
Joy-Mart	Supermarket	17
Shanghai Lianhua	Supermarket	2
	C-store	Over 100

Source: Hefei Commercial Bureau 2007

c. Carrefour

Carrefour, which has opened five stores in Anhui since April, 2006, including three in Hefei, has enjoyed sales far beyond original expectations. According to the manager of one branch in Hefei, the outlet sells more than 20,000 imported items. The manager emphasized that the snack food category is especially popular among young people and students, and that sales have increased dramatically in three successive years, partially due to increased purchasing power in this niche market, together with intensive on-site marketing activities. Sales of imported snack food sector SKUs have increased by more than 200% each year. Carrefour's Changjiang Rd. store is the most profitable and popular imported food shop among all foreign retailers. Its purchase manager stated that in-store promotions have been very effective in this market, and added that South Korean snack foods were successfully promoted last year.

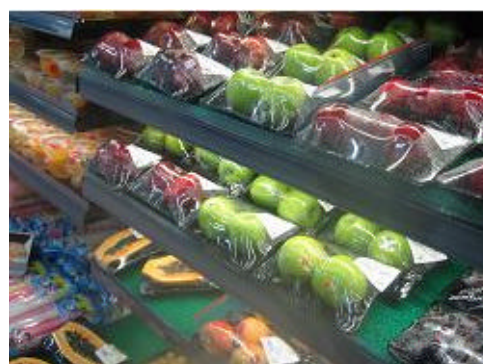


Imported food in Carrefour

d. Wal-Mart

The first Wal-Mart in Hefei opened in May 2008. The store is located in the city's commercial center, next to the famous Hilton Hotel. The majority of the store's goods are sourced domestically, with imported food accounting for about 5% of its total SKUs, comparatively less than the percentage found in other foreign operated retail stores.

During a store tour, we saw that U.S. food products were limited to only a few items: frozen potatoes, apples, oranges and dried fruits and nuts. A number of U.S. fruits such as Washington apples, California oranges, and grape are sold here, together with several condiments such as Heinz



Wal-Mart imported fruits

saucers and Tabasco brand pepper sauces. A few U.S. wines were included on the imported wine shelf. Since the shop is rather new, it is difficult to predict sales for specific items. Hefei's strong economy and increasing consumer demand makes Wal-Mart confident about its long-term position in the market, and Wal-Mart's second store in Hefei is planned to open soon.

II. U.S. Product Prospects in Hefei

ATO Shanghai conducted interviews with officers and executives from government institutions, HRI and retail and wholesale sectors. Overall, these sources revealed that current sales of imported foods are comparatively limited and that the local market is price sensitive. Nevertheless, retail giants like Metro, Wal-Mart, Carrefour, Lotus and Tesco have already entered this market and local high-end restaurants increasingly are using imported products, developments which should add to local familiarity with Western ingredients and condiments. These factors suggest future growth in the distribution of imported foods, and indicate a considerable potential for the development and market expansion of U.S. agricultural products. U.S. food products which could potentially grow in the Hefei market include the following:

Products	Markets	Notes
1. Potato products	HRI & Retail	<i>Increasingly popular and commonly used in fast-food and Western style restaurants and hotels; distribution is the primary obstacle; great potential for market expansion.</i>
2. Beef	HRI	<i>U.S. beef is using by some local restaurants, distributed through gray channels. Once the ban on imports is lifted, development potential will be high, though competition from Australian producers will remain significant.</i>
3. Table grapes	Retail	<i>Both U.S. red and black table grapes are visible in supermarkets. However, the market is price-sensitive, and distribution and logistics pose a major challenge.</i>
4. Fresh fruits	HRI & Retail	<i>Sunkist oranges and Washington apples already present and enjoy a considerable market share, retail sales are particularly strong, and market expansion potential should be high during the Spring Festival.</i>
5. Poultry	HRI & Retail	<i>U.S. frozen chicken wings occasionally</i>

		<i>appear on retail shelves. The most popular items are wingtips and feet.</i>
6. Condiments	HRI & Retail	<i>Tabasco and Heinz products are already present in local supermarkets, generally purchased by hotels and restaurants, with a considerable market expansion potential. However, there is strong competition from Spanish counterparts, whose products are more suitable to local consumer tastes.</i>
7. Wine	Retail & HRI	<i>Local market is currently dominated by French wines, while wines from Chile and Australia are also selling well, as a consequence of active promotions. U.S. brands such as Carlo Rossi wines, and Jack Daniels whiskey are already present in the market, and hotel chefs and retailers indicate a high potential for California wines as gifts items in imported food shops. More education for consumers and purchase managers is needed.</i>
8. Frozen products	HRI & Retail	<i>Frozen U.S. gold crisp onion rings and sweet corn are well-liked, while frozen mixed vegetables sales are not so good; local customers prefer fresh vegetables.</i>
9. Salmon	HRI & Retail	<i>Still a comparatively new product in this market, salmon is present on a seasonal basis, although most is imported from Norway at present, and salmon faces the same distribution problems as other seafood.</i>

10. Dairy products	HRI & Retail	<i>Popular and available here. Kraft Grated Parmesan cheese is a best selling item. U.S. dairy products are featured in Metro. Local retailers believe there is substantial demand for cheeses and butter, but competition from New Zealand and domestic products is strong.</i>
11. Dried fruits and nuts	Retail	<i>Already present in the market, retail sales are particularly strong. The main competition appears to be the sweet almonds and raisins from western China, Eighty-percent of U.S pistachio sales occur during the Spring Festival and enjoy a very decent market share.</i>

III. ATO Marketing Activity

A chef training program and seminar for purchase managers would be reasonable market activities to carry out in Hefei, according to high ranking managers from foreign retailers. ATO Shanghai is considering hosting a training program and seminar together with Metro which would take place at Metro's headquarters in Shanghai. Their professional kitchen facilities would be an ideal location to exhibit and showcase U.S. products and to be used for chef training courses.

IV. Contact Information and Useful Websites

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